October 4, 2021

VIA E-MAIL

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Alberta Securities Commission
Financial and Consumer Affairs Authority of Saskatchewan
Manitoba Securities Commission
Ontario Securities Commission
Autorité des marchés financiers
Financial and Consumer Services Commission of New Brunswick
Superintendent of Securities, Department of Justice and Public Safety, Prince Edward Island
Nova Scotia Securities Commission
Superintendent of Securities, Newfoundland and Labrador
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Re: CSA Position Paper 25-404 – *New Self-Regulatory Organization Framework*

Background

The Portfolio Management Association of Canada (**PMAC**) is pleased to have the opportunity to provide written feedback to the Canadian Securities Administrators (**CSA**) on CSA Position Paper 25-404 – *New Self-Regulatory Organization Framework*

(the **Position Paper**). PMAC represents over 300 investment management firms registered to do business with the various members of the CSA as portfolio managers (**PM**s). Approximately 65% of our members are also registered as investment fund managers (**IFM**s). Our members manage assets in excess of $2.9 trillion for institutional and private client portfolios; they range in size from one-person firms to large and bank-owned institutions, include traditional and online advisers, and operate domestically and internationally.

PMAC's mission statement is "advancing standards". We are consistently supportive of measures that elevate standards in the industry, enhance transparency, improve investor protection, and benefit our capital markets. We are also cognizant of the global market in which many of our mid-size and large members operate and are sensitive to any regulatory changes being misaligned with other international capital market jurisdictions.

PMAC takes no position on the decision to establish a new self-regulatory organization (**SRO**) to replace the Investment Industry Regulatory Organization of Canada (**IIROC**) and the Mutual Fund Dealers Association of Canada (**MFDA**), and to consolidate the two current investor protection funds (**IPFs**). We are strong supporters of good corporate governance and therefore have focused our recommendations on ways to strengthen CSA oversight of the new SRO and ensure the inherent conflicts of interest within an SRO structure are managed.

CSA Direct Regulation of Portfolio Managers and Investment Fund Managers

PMAC supports the continued direct regulation of PMs, EMDs and IFMs by the CSA. We understand the CSA's decision to focus on the merger of the two SROs and defer any consideration of incorporating other registration categories (PM, EMD, SPD) into the new SRO. As we stated in our response (**2020 Letter**) to the CSA Consultation Paper 25-402 *Consultation on the Self-Regulatory Organization Framework*, we are strongly opposed to delegating the regulation of PM and/or PM/EMD firms away from the CSA to the new SRO.

We have summarized the primary factors set out in our 2020 Letter supporting our position that PM firms should continue to be directly regulated by the CSA:

- Direct regulation of PMs by the CSA is and historically has proven to be extremely effective. CSA staff have the long-term experience and specialized expertise to understand the unique features of the PM business and the fiduciary duty of care owed by PMs to their clients;
- The CSA's principles-based approach to PM regulation provides the flexibility required to respond to and promote the wide variety of business models employed by PMs, whether they be investment counsellors, robo-advisers, family offices, global asset managers or large PM/IFMs. Many PMs are also registered as EMDs, usually for the purpose of managing and offering proprietary funds to clients of the PM – maintaining regulation of these

registration categories with the CSA will be more efficient and ensure a competitive Canadian market;

- The prescriptive nature of SRO regulation is inappropriate for, and incompatible with, the business models and client types served by PM firms, which include pensions, foundations and other institutional clients;
- PMs are subject to the highest proficiency standards in the industry and are fiduciaries to their clients, with a duty to act in clients' best interests. A "one-size-fits-all" model of regulation carries the risk of proficiencies being lowered over time;
- Direct CSA regulation is more in line with international regulation, which is predominantly principles-based, direct government regulation in other jurisdictions. Any shift to a prescriptive, self-regulatory model and rules-based regulation would put Canadian PM registrants at a significant competitive disadvantage globally;
- Many PM firms are also registered as IFMs and/or EMDs. Approximately 65% of PMAC members are both PMs and IFMs, and many are part of international firms. PMs and IFMs are closely intertwined – dividing their regulation between the new SRO and the CSA would increase costs and regulatory burden, which is not in the best interests of investors and runs counter to the overall objective of SRO consolidation;
- Direct regulation is strong regulation and better serves the investing public by minimizing conflicts of interest and other inherent problems with the SRO model. No market or investor protection reasons have been raised in support of delegating PM regulation to an outside body.

We believe that a failure to acknowledge the differences in registration categories, advice model and duty to investors could result in inappropriately prescriptive regulation that impedes a PM's professional judgement, hampers competition and innovation and, over the long term, does not benefit investors.

We look forward to responding to a future consultation regarding the regulation of PM firms in Phase 2 of the implementation process. We will restrict our comments to the proposed changes that will occur during Phase 1 described in the Position Paper.

KEY RECOMMENDATION

CSA oversight of the new SRO should be significantly strengthened

We are very pleased with many of the suggested SRO governance and oversight reforms proposed in the Position Paper. We appreciate that the CSA took stakeholder feedback into consideration and made significant efforts to adopt an investor protection lens in developing these proposals. However, there are some instances

where we believe the CSA should take a more active role in its oversight of the new SRO, as discussed below.

We have the following specific comments on various aspects of the Position Paper. Our comments are set out in blue in the order and under the headings they appear in the Position Paper. We have omitted those sections where we have no comments.

a) Improving Governance

Clear communication of public interest mandate

The New SRO will clearly convey how the public interest informs the New SRO's regulatory actions and responsibilities, specifically by:

- Emphasizing the public interest mandate in the ROs, by-laws, and other applicable constating documents of the New SRO.

  PMAC agrees that investor protection and the public interest must be the primary mandate and focus of regulators, including SROs. The public interest mandate should permeate the culture of the SRO, including the selection of candidates to fill Board, senior management and staff positions. The definition of the "public interest" should be determined by the CSA.

  We believe that SRO officers and directors must be held to at least the same ethical and conduct standards (including those related to conflicts of interest) applicable to CSA Members (Commissioners).

- Requiring the New SRO to inform stakeholders of its public interest mandate and corporate governance structure, rulemaking processes and enforcement processes. We agree.

- Requiring training to directors, board committee members, senior management, and staff in interpreting its public interest mandate, to ensure alignment of the public interest between the New SRO, statutory regulators, and governments.

  We agree that this is an effective way to emphasize the paramountcy of the public interest.

- Requiring the New SRO to describe the public interest impact of rule proposals, guidance and policies published for comment. We agree.

- Requiring the compensation structure for New SRO executives to be linked to the delivery of the New SRO's public interest mandate.

  We also agree that this is likely to maintain a focus on the public interest within the organization.

New SRO board composition

- Requiring a majority of the New SRO's directors to be independent.

  PMAC agrees that the majority of the SRO's board of directors should be independent. As we noted in our 2020 Letter, we believe that industry directors should not represent more than one third of any SRO board.

- Requiring that the Chair of the New SRO board be an independent director and that the roles of Chief Executive Officer (CEO) and Chair be occupied by separate persons. We agree.

- Requiring that the Governance / Nominating committee of the board be composed entirely of independent directors and requiring that the Chairs of other committees such as Audit, Human Resources, etc. be independent. We agree

- Requiring that a reasonable proportion of New SRO directors have relevant experience regarding investor protection issues (as has already been implemented by IIROC).

  We believe that most, if not all, SRO directors should have investor protection experience, and that this should be a significant factor in appointment decision-making. In addition to directors having investor protection experience, we believe that investors must be independently represented on the board of the SRO. These measures will demonstrate a firm commitment to the SRO's investor protection mandate.

- Providing a CSA non-objection process grounded in principles-based considerations for all independent directors, including:

  We do not see the policy reasons for limiting the proposed CSA non-objection process to independent directors; we are of the view that all directors should be appointed jointly by CSA member jurisdictions.

  - a mechanism for the New SRO to undertake due diligence and other governance best practices such as the use of evergreen lists and development of board skills matrices that would take into account the attributes or backgrounds needed for a balanced board, including

considering board diversity in terms of (i) director-type and (ii) geographic board representation, which will ensure an equitable balance of interests;

- a mechanism for the CSA to review the initial matrices and any subsequent changes to them, including a reporting requirement in the RO for material change to the matrices; and

  We do not believe that a "review" of matrices developed by the SRO goes far enough. Instead, the CSA should be directly involved in the appointment of all directors, including the development and approval of any selection criteria.

- Requiring that appropriate cooling-off periods commensurate with governance best-practices for CSA regulators be considered for any independent director positions.

  We disagree with the notion of a "cooling-off" period for independent directors. It would be preferable if anyone previously employed in the securities industry is excluded from consideration as an "independent" director.

- Maintaining a workable board size for the New SRO of not more than 15 directors (including the CEO), subject to change with CSA approval. We agree.

- Maintaining appropriate term limits for the New SRO board members and extending these term limits to the CEO.

  We agree and suggest term limits of 9 years, with no allowance for legacy directors to have their terms extended. We also believe that key executive positions should be subject to term limits.

- Requiring the New SRO to develop diversity and inclusion policies aimed at increasing underrepresented groups on the board. We agree.

Independence criteria for independent directors

- Requiring the New SRO to create, in consultation with the CSA, criteria to assess the independence of directors annually (e.g., affiliations with industry associations).

  We agree that the independence of directors should be annually assessed according to pre-determined criteria. We believe the CSA should approve the criteria. As we noted in our 2020 Letter, we think that conflicts of interest policies and codes of conduct should be independently audited.

- Ensuring that independence requirements for New SRO directors are at least comparable to those for directors of public companies (as provided for in National Instrument 52-110 Audit Committees (NI 52-110), with necessary adaptations), including appropriate cooling-off periods. It is recognized that the context of NI 52-110 is different from the SRO context and that other prerequisites will be considered in determining the appropriate independence requirements for the directors of the New SRO.

  As noted above, we do not agree with the notion of "cooling-off" periods if directors are to be truly independent.

Formal investor advocacy mechanisms

- Requiring the New SRO to establish an investor advisory panel to provide independent research or input to regulatory and/or public interest matters (potentially financed through a restricted fund). The Working Group acknowledges that IIROC has made public statements of their intention to establish a similar expert investor issues panel. We agree.

- Requiring the New SRO to create a mechanism to formally engage directly with investor groups (on an advisory basis) to obtain broader input on the design and implementation of applicable policy proposals and rulemaking. We agree.

- Requiring regulatory policy advisory committees to include a reasonable proportion of investor / independent / public representatives. We agree.

CSA involvement in new SRO corporate governance

- Requiring the New SRO to engage with the CSA regarding the appropriateness of the nominees for independent directors and providing for a CSA non-objection to such nominees, selected through a fit and proper assessment process.

  As noted above, we do not see the policy rationale for limiting CSA engagement to independent directors, and believe that the CSA should be responsible for appointing all SRO directors.

- Providing for a CSA non-objection process for the appointment of the CEO, including a requirement for the New SRO to develop a sub-matrix of appropriate criteria to inform the non-objection process.

  We are of the view that the CSA should have the ability to veto all key appointments, including the Chair and the CEO. We believe that the criteria to inform the non-objection process should be determined by the CSA, not the SRO, or at minimum, that it should be subject to CSA approval.

- Clarifying existing authority in an appropriate governing document, as applicable for each CSA jurisdiction, to direct the New SRO to enact, amend, or repeal, either in whole or in part, any by-law, rule, regulation, policy, prescribed form, procedure, interpretation or practice. We agree.

- Enabling a specific by-law provision for the New SRO requiring that a director of the board be terminated from that position if the director no longer meets the relevant fit and proper criteria (e.g., Code of Ethics) as established by the New SRO and approved by the recognizing regulators. We agree.

CSA oversight

- Enabling CSA review / non-objection process for member exemptions brought to the board of the New SRO. We agree.

- CSA publication of an annual activities report on the CSA's oversight of the New SRO and New IPF. We agree.

- Consideration of annual meetings between the CSA Chairs and the Chair of the New SRO as well as the Chairs of the New SRO's board committees. We agree.

- Ensuring that the New SRO's RO includes appropriate general requirements regarding the adequacy and location of New SRO staff / executives / board directors. We agree.

- A specific reporting requirement in the RO to refer escalated complaints about the New SRO by members or others under its jurisdiction to the CSA. We agree.

- Codifying within the new RO a requirement that the New SRO solicits CSA comments and input on annual priorities, strategic plans and business plans (including budget); and that the CSA maintains a non-objection mechanism, including over significant future publications and communications.

  We agree that the SRO annual priorities, strategic plans and business plans (including budget) should be submitted to the CSA for comment and input, but we believe they should also be subject to CSA approval. We agree that the CSA should have the ability to veto any significant publications, including guidance or rule interpretations.

Other solutions

- Transferring all current IIROC District Council regulatory decision-making functions to the board and staff of the New SRO. IIROC District Councils and MFDA Regional Councils will retain their advisory role with respect to regional issues, as well as the provision of regional perspective on national issues. This

would involve ensuring an escalation mechanism within the New SRO as applicable. We agree.

- Requiring that all directors of the New SRO receive mandatory annual training on industry, governance, and investor protection issues, including training on their specific role and responsibilities within the corporate governance structure in support of the public interest mandate and the management of conflicts of interest. We agree.

- Requiring independent directors of the New SRO to have a separate "in camera" session at board meetings. We agree.

- Requiring the board of the New SRO to meet with the proposed investor advisory panel at least annually in addition to meeting with executives. We agree.

b) Strengthening Proficiency

- Consider proposing more nuanced proficiency-based registration categories to ensure consistent quality of standards for clients.

  As we noted in our 2020 Letter, new products, services and methods of delivery are continuously being introduced to the marketplace. The regulatory framework must be flexible to evaluate and regulate new products, services and delivery methods as they emerge. More importantly, industry participants must understand the products they offer and the implications of how they deliver their services.

  In the consultations that gave rise to the CFRs, PMAC called for a fiduciary standard of care across the industry. However, many industry participants rejected not only the fiduciary standard, but also the proposed regulatory best interest standard. As a result, we are concerned that without appropriate vigilance, standards may be pulled downward across the industry. All regulators must require the same high standards from registrants.

  To best serve the public interest, it is key that proficiency and regulatory standards remain high, regardless of the product, and regardless of the consumer demographic. There should be as much harmonization as possible in terms of product and distribution standards across various types of registered firms. All investors are entitled to expect their investment service provider to have appropriate proficiency and to act with integrity.

  In our view, the wider the variety of products offered by a registrant, the higher the proficiency standards should be. It is our belief that anyone offering

discretionary advice must have the highest level of proficiency and be subject to a fiduciary duty.

More than establishing registration categories and required proficiency, investor protection requires effective compliance oversight and addressing registrant misconduct. Products and services change rapidly, and the regulatory framework must have the flexibility to adapt to ensure consumer protection.

- Leverage ongoing and future work on proficiency standards, titles and designations that is part of the broader CSA Client Focused Reforms project. We agree.

- The New SRO to continue to promote the merits of additional credentials for individual registrants (e.g., so that they are better equipped to provide more holistic advice to their clients on financial concepts, planning for financial goals, budgeting or debt management, tax and estate planning). We agree

c) Enhancing investor education

- The establishment of a separate investor office within the New SRO that is prominently positioned and supports policy development and is easily identifiable and accessible to investors. We agree.

- Funding the aforementioned investor education or outreach activities through a new requirement in the New SRO budget or a specific part of the restricted fund.

  We agree. We also support continued investor education initiatives and behavioural research studies, such as those undertaken recently by the OSC.

- Adding specific terms and conditions to the RO to require, to the extent possible, public transparency in enforcement notices in respect of processes for assessing firm supervision and reasons for disciplinary decisions. We agree.

- Reviewing the New SRO sanction guidelines / policies on the public disclosure of credit for cooperation, specifically for the inclusion and consideration of compensation to clients harmed by misconduct as a mitigating factor (or an aggravating factor if inadequate compensation was provided) in assessing appropriate sanctions. We agree.

  We also encourage enhanced investor education regarding the establishment of the new SRO. There has been a great deal of coverage in the media regarding the future of the SROs and the SRO framework, and continued

information and transparency will be important to keep investors informed about the coming changes.

f) Fostering Harmonization/Efficiencies

- As outlined in section 3 of this Position Paper, the IWC will oversee a policy review of the existing IIROC and MFDA rule books / guidance to increase harmonization of similar rules, as well as their interpretation and application. The focus will be to identify differences in the rules / guidance, arbitrage opportunities and overlaps, and propose either (i) to maintain necessary differences, or (ii) seek appropriate amendments to harmonize or eliminate regulatory gaps.

  As part of this policy initiative, the IWC will consider the following:
  - harmonized interpretation of rules with securities legislation (e.g., Client Focused Reforms);
  - guidance that clearly articulates the intended outcomes for rules;
  - rules that are scalable or proportionate to the different types and sizes of member firms and their respective business models;
  - assessment of the economic impact of proposed rule changes to affected stakeholders;
  - harmonization of rules that individually may require unnecessary technological systems or processes; and
  - identifying improvements to internal processes (e.g., for SRO examination reports, as applicable, to reference guidance to assist firms in improving outcomes).

  We agree that the working group should complete a comprehensive policy review of the existing IIROC and MFDA rules and guidance to increase harmonization of the rules, their interpretation and application. We agree that the review should focus on intended outcomes.

  As noted in our 2020 Letter, in order to curb issues of regulatory arbitrage, we urge the CSA to carefully consider the public interest and investor outcomes in determining what changes may be required with respect to the regulatory tools available to the SRO, its deployment of those tools and the CSA's oversight of the SRO's business compliance and enforcement functions.

  Regulators should have access to similar tools, and these should be employed in a similar manner by all regulators. The CSA should design its SRO oversight program to evaluate whether the tools are being employed uniformly. This includes whether compliance deficiencies, including significant and/or repeat deficiencies, are being appropriately dealt with at the firm level.

- To foster harmonization between the New SRO and the CSA, require the New SRO to solicit CSA comment and input on annual priorities and business plan (including budget); and furthermore, the CSA to maintain a non-objection mechanism, including over significant future publications and communications.

  As noted above, we are of the view that the CSA should approve the SRO's annual priorities and business plan (including budget), and significant publications including rules and guidance.

- To assist investors in effectively navigating the complaint resolution processes, review existing regulatory processes across channels with the intent to:
  - centralize the complaint reporting process and explore the merits of creating a single complaint filing portal for the New SRO through which investors could use a standard complaint form to file all types of complaints which the portal would then consolidate, filter and route to the appropriate organization (e.g., the registered firm, internally within the New SRO, appropriate CSA member, OBSI);
  - apply a consistent complaint handling process to review and investigate all types of complaints;
  - develop and apply service standards for complaint resolution; and
  - consider the merits or feasibility of allowing client / victim impact statements for consideration by a hearing panel during the sanction proceedings.

  In the longer term, consideration will be given to expanding the process to include a single complaint filing portal for all registration categories, integrating current CSA processes.

  We agree that the complaint reporting process should also be reviewed, and that a single complaint filing portal should be considered. We will provide any comments we have with respect to whether the single filing portal should include firms in other registration categories, in the planned Phase 2 consultation.

- Given the similarities in coverage for the IPFs, to alleviate investor confusion and to facilitate an improved understanding of the role of investor protection funds, consolidate CIPF and the MFDA IPC into a single protection fund that is independent from the New SRO. An appropriate governance structure for this New IPF will be considered as well.

  The New IPF will review and propose changes to its policies related to disclosure, coverage and claims, focusing on improving plain language disclosure. Furthermore, until any proposed changes are approved, the New IPF would be required to maintain separate coverage pools for investment and

mutual fund dealers. Initially maintaining separate coverage pools will enable the consolidated protection fund to conduct a proper assessment of insolvency risks for the different types of dealers. Until the assessment is complete, a moratorium on any change to the methodology, applied to fees or assessments that would result in a material increase in applicable IPF fees without CSA authorization, will apply.

In the second phase, when consideration is given to assessing the feasibility of incorporating other registration categories within the one SRO framework, consideration will also be given to the possibility of providing coverage to clients of the other registration categories and harmonizing the consolidated protection fund with the Fonds d'indemnisation des services financiers in Québec.

We have no comment on the consolidation of the existing IPFs. We will provide any comments we have with respect to whether IPF coverage should be expanded to include firms in other registration categories, in the planned Phase 2 consultation.

g) Harmonizing Directed Commissions

Our only comment with respect to this section of the Position Paper is that we believe the working group should consider the potential consequences of allowing registrants to use personal corporations, such as whether the corporation may be used to conduct Outside Business Activities, and whether registrants may use corporate titles that could be misleading to investors.

i) Leveraging Ongoing Related Projects

Consolidation of databases and harmonization with insurance regulators

- The CSA SEDAR+ project which will improve the CSA's national consolidated database and enhance public disclosure of registered firms and individuals in one portal, including historical disciplinary information of active or former registrants. Regulatory staff involved in the project should consider the merits of including public disclosure and easy access to information pertaining to registrants similar to that contained in the SEC's Form ADV, or the current IIROC Advisor Report.

- The CSA initiative with the Canadian Council of Insurance Regulators on full cost disclosure and performance reports.

  We agree. In our 2020 Letter, we urged the creation of a national registration regime and a database that can be used by investors to determine where and in what capacity their financial services provider is registered; to be effective, we believe that this database should include historical disciplinary information in plain language so that retail investors are able to understand the nature of the registrant's conduct / omission.

The improvement of systems such as SEDAR+ and making such information available in a user-friendly and accessible manner to the public would be an important step in increasing investor information.

Conclusion

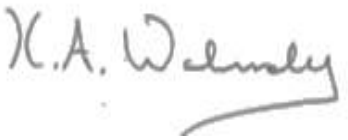
We are very pleased that the CSA has taken this opportunity to improve investor protection and market efficiency by proposing measures that will significantly strengthen the governance and oversight of the new SRO.

We will continue to advocate that PMs and EMDs that are also registered as PMs should continue to be directly regulated by the CSA; we believe that direct government regulation is stronger regulation and is more appropriate for discretionary managed accounts guided by a fiduciary duty. A move towards more prescriptive rules-based regulation in the PM sector would add regulatory burden and have a significant negative impact on the competitiveness of the Canadian asset management industry.

We would be pleased to discuss any of our comments with you at your convenience. Please do not hesitate to contact Katie Walmsley at (416) 504-7018 or Victoria Paris at (416) 504-7491.

Yours truly,

PORTFOLIO MANAGEMENT ASSOCIATION OF CANADA



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